Platinum sector suffers chronic underinvestment

The South African mining sector is suffering from lack of investment, falling head- grades, strike action, political strife and overall poor productivity. The platinum sector is suffering the same plight with the added issue of lower recycling rates and reduced market share of diesel cars.

In our opinion, the lack of investment in South African mining has little chance of reversing in the medium term, if at all. Our sentiment has been echoed in recent weeks by CEO's of South African platinum companies which is the largest source for platinum used in autocatalyst devices.

The World Platinum Investment Council adjusted its supply deficit forecast for 2016 upwards to 520,000 ounces from the prior estimate of 455,000 ounces. The increase cited lower than expected recycling growth and represents the fifth consecutive year of undersupply.

Implats' CEO indicated that they are forecasting South Africa's platinum supply to drop to below 3m ounces by the end of the decade and even if investment was made available, there would be too little time to bring new mines into production which takes decades.

Northams revealed that South African output would total just over 4m ounces in 2017, falling from 5.6m ounces in 2006. Out of this, around 5.5m ounces is expected to be needed for industrial use from the total demand of 8.7m ounces. As such, the company is planning to bring on an additional 800,000oz over the next six years to coincide with the increased demand.

Whilst the future demand/ supply imbalance is indisputable, the fact that a mine would take around 15 years to bring into production and to realise a return on investment has made it harder to attract investment as investors would have to be convinced of the long term sustainability of the industry.

In 2015, 2.25m ounces of platinum was used in the light duty diesel vehicle market and some 520,000 ounces and 250,000 ounces for heavy duty trucks and non-road vehicles respectively. Platinum demand is therefore reliant on the health of the diesel sector. With regards to heavy duty trucks, given that there are financial advantages to using more efficient diesel trucks over gasoline, diesel trucks should remain dominant and platinum demand to this sector could more than double by the end of the decade.

The outlook for the light duty trucks or passenger vehicle sector is more uncertain. New emission standards in Europe will require more complex emissions aftertreatment. This should result in an increase in the price of a typical diesel vehicle compared to gasoline equivalent, resulting in diesel engines losing some market share. It is unclear whether this decline in market share could potentially be offset by an increase in the amount of platinum required per car or truck in order to accommodate the cleaner emission standards. If this were the case, then the overall demand for platinum in this sector could potentially increase. However, until we have clarity around this potential, it will be hard to convince investors to develop new mines, especially for a return that will not be realised for more than a decade.

As such, investors remain cautious and the larger players are considering their respective strategies. Lonmin has stopped all loss-making mines and has not yet restarted its K4 mine which will deliver a low-cost platinum resource in Rustenburg. Anglo Platinum has switched its strategy to mining shallow, mechanised mines selling its deep level mines to Sibanye Gold. Sibanye will require large capital investment in order to produce platinum which is uncertain at this stage. Impala intends to replace its output from old mines with the development of 17 new shafts over the next few years, though currently the board has not expedited the deployment of these shafts.